

Lincoln County Rural Water District No. 3
Lincoln County, Oklahoma
For the Year ended December 31, 2012 and 2013

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INDEPENDENT AUDITOR'S REPORT

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Board of Directors
Lincoln County Rural Water District No. 3
Wellston, Oklahoma

I have audited the accompanying financial statements of the business-type activities of Lincoln County Rural Water District No. 3, Lincoln County, Oklahoma, as of and for the year ended December 31, 2012, and December 31, 2013, and the related notes to the financial statements, which collectively comprise Lincoln County Rural Water District No. 3, Lincoln County, Oklahoma's basic financial statements as listed on the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the modified cash basis of accounting described in Note 2. This includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to error or fraud.

Auditor's Responsibility

My responsibility is to express opinions on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion

on the effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinions.

Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position-modified cash basis of the business-type activities of Lincoln County Rural Water District No. 3, Lincoln County, Oklahoma, as of December 31, 2012, and December 31, 2013, and the respective changes in financial position-modified cash basis and cash flows thereof for the years ended, in conformity with the basis of accounting described in Note 2.

Basis of Accounting

I draw attention to Note 2 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the modified cash of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. My opinion is not modified with respect to that matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, I have also issued my report dated October 14, 2014, on my consideration of the District's internal control over financial reporting and my tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of audits performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of my audit.



Bill Ford, C.P.A.

October 14, 2014

LINCOLN COUNTY RURAL WATER DISTRICT No. 3
LINCOLN COUNTY, OKLAHOMA
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
DECEMBER 31, 2012 and 2013

<u>ASSETS</u>	<u>2012</u>	<u>2013</u>
Current assets:		
Cash and cash equivalents	\$ 77,844	\$ 63,088
Total current assets	<u>77,844</u>	<u>63,088</u>
Restricted assets:		
Cash and cash equivalents	<u>30,394</u>	<u>30,394</u>
Total restricted assets	<u>30,394</u>	<u>30,394</u>
Non-current assets:		
Deferred debt expense, net	6,403	6,136
Capital assets:		
Land	6,190	6,190
Other capital assets, net of accumulated depreciation	<u>1,182,250</u>	<u>1,171,222</u>
Total non-current assets	<u>1,194,843</u>	<u>1,183,548</u>
Total assets	<u>\$1,303,081</u>	<u>\$1,277,030</u>
<u>LIABILITIES</u>		
Current liabilities:		
Payroll taxes	718	718
Notes payable, current	<u>9,462</u>	<u>9,967</u>
Total current liabilities	<u>10,180</u>	<u>10,685</u>
Non-current liabilities:		
Notes payable, non-current	<u>396,575</u>	<u>386,608</u>
Total non-current liabilities	<u>396,575</u>	<u>386,608</u>
Total liabilities	<u>406,755</u>	<u>397,293</u>
<u>NET ASSETS</u>		
Nonspendable capital assets, net of related debt	782,376	780,837
Restricted for debt service	30,394	30,394
Unassigned	<u>83,556</u>	<u>68,506</u>
Total net assets	<u>\$ 896,326</u>	<u>\$ 879,737</u>

See accompanying notes to financial statements

LINCOLN COUNTY RURAL WATER DISTRICT No. 3
LINCOLN COUNTY, OKLAHOMA
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES
IN FUND NET ASSETS - MODIFIED CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2012 and 2013

<u>Operating Revenues</u>	<u>2012</u>	<u>2013</u>
Charges for services:		
Water charges	\$ 156,689	\$ 146,961
Other	<u>10,596</u>	<u>10,825</u>
Total operating revenues	<u>167,285</u>	<u>157,786</u>
<u>Operating Expenses</u>		
Purchased water	48,719	47,192
Salaries	30,000	30,000
Utilities	1,730	2,602
Operating supplies	11,081	7,113
Repairs and maintenance	7,245	4,542
Water samples	294	3,282
Telephone expense	3,229	2,963
Office supplies	2,977	3,667
Insurance and bonds	6,693	6,435
Professional fees	2,000	2,000
Dues, fees, and permits	606	599
Travel	5,595	6,144
Payroll taxes	2,295	2,295
Other expenses	103	32
Amortization	267	267
Depreciation	<u>34,316</u>	<u>34,681</u>
Total operating expenses	<u>157,150</u>	<u>153,814</u>
Operating income (loss)	<u>10,135</u>	<u>3,972</u>
<u>Non-operating Revenue (Expenses)</u>		
Interest income	438	348
Interest on notes payable	<u>(21,388)</u>	<u>(20,909)</u>
Total non-operating revenue (expenses)	<u>(20,950)</u>	<u>(20,561)</u>
Income (loss) before contributions and transfers	<u>(10,815)</u>	<u>(16,589)</u>
Loss on sale of assets	<u>(3,168)</u>	<u>0</u>
Capital contributions	<u>0</u>	<u>0</u>
Change in net assets	<u>(13,983)</u>	<u>(16,589)</u>
Total net assets, beginning	<u>910,309</u>	<u>896,326</u>
Total net assets, ending	<u>\$896,326</u>	<u>\$ 879,737</u>

See accompany notes to the financial statements

LINCOLN COUNTY RURAL WATER DISTRICT No. 3
LINCOLN COUNTY, OKLAHOMA
STATEMENTS OF CASH FLOWS - MODIFIED CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2012 and 2013

<u>Cash Flows from Operating Activities</u>	<u>2012</u>	<u>2013</u>
Cash received from members and others	\$ 167,285	\$ 157,786
Cash paid to suppliers and employees	<u>(122,567)</u>	<u>(118,866)</u>
Net cash provided (used) by operating activities	<u>44,718</u>	<u>38,920</u>
 <u>Cash Flows from Capital and Related Financing Activities</u>		
Principal paid on notes payable	(8,984)	(9,463)
Interest paid on notes payable	(21,388)	(20,909)
Net cash provided (used) by capital & related financing activities	<u>(30,372)</u>	<u>(30,372)</u>
 <u>Cash Flows from Investing Activities</u>		
(Increase) decrease in restricted assets	(2)	0
Interest earned	438	348
(Acquisition) disposition of capital assets	<u>(3,186)</u>	<u>(23,653)</u>
Net cash provided (used) by investing activities	<u>(2,750)</u>	<u>(23,305)</u>
Net increase (decrease) in cash and cash equivalents	11,596	(14,757)
Cash and cash equivalents, beginning	<u>66,248</u>	<u>77,844</u>
Cash and cash equivalents, ending	<u>\$ 77,844</u>	<u>\$ 63,088</u>
 <u>Reconciliation of operating income (loss) to net cash provided (need) by operating activities:</u>		
Operating income (loss)	\$ 10,135	\$ 3,972
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Amortization	267	267
Depreciation	34,316	34,681
Increase (decrease) in payroll taxes	<u>0</u>	<u>0</u>
Total adjustments	<u>34,583</u>	<u>34,948</u>
Net cash provided (used) by operating activities	<u>\$ 44,718</u>	<u>\$ 38,920</u>

See accompanying notes to financial statements

LINCOLN COUNTY RURAL WATER DISTRICT No. 3
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012 and 2013

1. ORGANIZATION

Lincoln County Rural Water District No. 3 (the District) was organized under Title 82, §1324.1 *Oklahoma Statutes*, on October 24, 1988, as a political subdivision of Lincoln County, Oklahoma. The District supplies water to member users living within the district and constructs and maintains all water lines and other related property and equipment.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Significant accounting and reporting policies applied in the preparation of the accompanying financial statements for the year ended December 31, 2012 and 2013, are as follows:

Government-Wide and Fund Financial Statements - The District is a special purpose governmental entity engaged only in business type activities. The District prepares financial statements required for enterprise funds.

Measurement Focus and Basis of Accounting - Measurement focus is a term used to describe “how” transactions are recorded within the various financial statements. Basis of accounting refers to “when” transactions are recorded regardless of the measurement focus applied.

Measurement Focus:

In the financial statements business-like activities are presented using the economic resources measurement focus, within the limitations of the modified cash basis of accounting. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows. All assets and liabilities (whether current or non-current, financial, or non-financial) associated with their activities are reported. Fund equity is classified as net assets.

Basis of Accounting:

In the financial statements, business-like activities are presented using a modified cash basis of accounting. This basis recognizes assets, liabilities, net assets/fund equity, revenues, and expenditures/expenses when they result from cash transactions with a provision for depreciation. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As a result of the use of this modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements. If the District utilized the basis of accounting recognized as generally accepted, the financial statements would use the accrual basis of accounting.

Fund Types and Major Funds - The District reports all activity within a single fund.

Property and Equipment - Acquisition and construction costs of property and equipment are capitalized, and depreciation is provided on a straight-line basis over the estimated useful lives of the property and equipment as follows:

<u>Type of Assets</u>	<u>Years</u>
Water line system	50
Building and improvements	20
Fencing	10
Equipment and truck	5

Contributed Capital - Amounts received by the District from member units and proceeds received as contributions in aid of construction from other entities as grants are recorded as contributed capital.

Use of Estimates - Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets, liabilities, and equity, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

Debt Issuance Costs - Debt issuance costs are deferred and amortized over the term of the debt using the straight-line method, which approximates the effective interest method.

Income Tax Status - The District is a political instrumentality of Lincoln County, Oklahoma, and therefore, exempt from income taxes under the *Internal Revenue Code*.

Compensated Absences - Personal leave in varying amounts are granted by the District. The District does not record a liability for accrued compensated absences. Using the modified cash basis the amount paid for compensated absences is expensed as paid.

3. CASH AND INVESTMENTS

The District's investment policies are governed by state statute. Permissible investments include direct obligations of the United States Government and Agencies; certificates of deposit of savings and loan associations, and bank and trust companies; and savings accounts or savings certificates of saving and loan associations, and trust companies. The District considers highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Collateral is required for demand deposits and certificates of deposit for all accounts not covered by federal deposit insurance.

Deposits and Investments - The District's cash deposits and investments at December 31, 2012 and 2013, were completely insured by federal deposit insurance. Therefore, the District's cash deposits and investments at December 31, 2012 and 2013, were not exposed to Custodial Credit Risk, Investment Credit Risk, Investment Interest Rate Risk, or Concentration of Investment Credit Risk.

4. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2012 and 2013, were as follows:

	Balance 1/1/12	Decreases/ Increases 2012	Decreases/ Increases 2013	Balance 12/31/13
Capital assets not being depreciated:				
Land	\$ 6,190			\$ 6,190
Total capital assets not being depreciated	6,190			6,190
Other capital assets:				
Water line system	\$1,636,683		23,653	\$1,660,336
Building/improvements	7,736	26,457		34,193
Fencing	3,000			3,000
Equipment and truck	27,656			27,656
Total other capital assets	1,675,075	26,457	23,653	1,725,185
Total capital assets	1,681,265	26,457	23,653	1,731,375
Less accumulated depreciation for:				
Water line system	454,610	32,734	32,971	520,315
Building/improvements	3,870	(2,588)	1,710	2,992
Fencing	2,700	300	0	3,000
Equipment and truck	27,656	0	0	27,656
Total accumulated depreciation	488,836	30,446	34,681	553,963
Capital assets, net	\$1,192,429	\$ (3,989)	\$(11,028)	\$1,177,412

Depreciation expense for the year ended December 31, 2012 and 2013, were \$34,316 and \$34,681, respectively. The above investment for water lines includes interest capitalized during construction of \$19,887.

5. DEBT ISSUANCE COSTS

During the year ended December 31, 1997, the District paid \$10,675 in legal fees related to issuing debt in conjunction with building a water line. These legal fees have been capitalized and are being amortized over the life of the loans. For the years ended December 31, 2012 and 2013, \$267 in amortization expense were recognized.

6. LONG-TERM DEBT

The District had the following long-term debt as of December 31, 2012 and 2013:

Notes Payable:	<u>2012</u>	<u>2013</u>
Note 91-01, U.S. Department of Agriculture - Rural Development dated October 31, 1995, for the amount of \$442,500. Payments of \$2,244 per month for 40 years including interest at 5.25%. Secured by all business assets.	\$357,020	\$348,636
Note No. 91-03, U.S. Department of Agriculture - Rural Development, dated May 28, 1997, for the amount of \$60,000. Payments of \$287 per month for 40 years including interest at 4.875%. Only interest - no principal - was paid the first year. Secured by all business assets.	<u>49,017</u>	<u>47,939</u>
Total Long-Term Debt	<u>\$406,037</u>	<u>\$396,575</u>

Changes in long-term debt during the year ended December 31, 2012 and 2013, were as follows:

	Balance at 1/1/12	Decreases	Balance at 12/31/12	Decreases	Balance at 12/31/13
Note 91-01-Rural Development	\$364,981	\$ (7,961)	\$357,020	\$(8,384)	\$348,636
Note 91-03-Rural Development	<u>50,045</u>	<u>(1,028)</u>	<u>49,017</u>	<u>(1,078)</u>	<u>47,939</u>
Total notes payable	<u>\$415,026</u>	<u>\$ (8,989)</u>	<u>\$406,037</u>	<u>\$(9,462)</u>	<u>\$396,575</u>

Annual payments required to amortize the above outstanding debt over the next five years and thereafter, are as follows:

Year Ended <u>12/31</u>	Note 91-01 <u>Rural Development</u>		Note 91-03 <u>Rural Development</u>		Total <u>Notes Payable</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2013	\$ 8,384	\$ 18,544	\$ 1,078	\$ 2,366	\$ 9,462	\$ 20,910
2014	8,835	18,093	1,132	2,312	9,967	20,405
2015	9,310	17,618	1,188	2,256	10,498	19,874
2016	9,811	17,117	1,248	2,196	11,059	19,313
2017	10,338	16,590	1,310	2,134	11,648	18,724
2018	10,894	16,034	1,375	2,069	12,269	18,103
Thereafter	<u>291,044</u>	<u>151,515</u>	<u>40,628</u>	<u>21,340</u>	<u>331,672</u>	<u>172,855</u>
	<u>\$348,616</u>	<u>\$255,511</u>	<u>\$47,959</u>	<u>\$34,673</u>	<u>\$396,575</u>	<u>\$290,184</u>

7. COMPENSATED ABSENCES

The District has not reported an amount for accrued compensated absences. Under the modified cash basis of accounting, payments for vacation and sick leave are expensed as paid.

8. RESERVE ACCOUNT

Section 4(d) of the loan agreement with Rural Development stipulates that the District establish a reserve account for repairs and replacement of the system. An amount equal to ten (10%) percent of the monthly debt service payments shall be transferred monthly to the reserve account until the balance reaches an amount equal to the annual debt service payments, or \$30,372.

The reserve account, including accumulated interest earned thereon, is shown as restricted cash on the statement of net assets - modified cash basis. The respective balances of the reserve account as of December 31, 2012, and 2013 are \$30,394.

9. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The District carries commercial insurance for risk of loss, including workers' compensation.

10. CONTRACTS

The District purchases water for resale from the Chandler Municipal Authority, Chandler, Oklahoma. The price paid by the District is determined based on costs incurred by the Authority in producing the water purchased. The contract contains terms defining the costs to be considered.

11. SUBSEQUENT EVENTS

Subsequent events have been evaluated through October 14, 2014, which is the date the financial statements were available to be issued.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS

Board of Directors
Lincoln County Rural Water District No. 3
Wellston, Oklahoma

I have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, the financial statements-modified cash basis of the business-type activities of Lincoln County Rural Water District No. 3, Lincoln County, Oklahoma, as of and for the year ended December 31, 2012, and December 31, 2013, and the related notes to the financial statements, which collectively compromise Lincoln County Rural Water District No. 3, Lincoln County, Oklahoma's basic financial statements and have issued my report thereon dated October 14, 2014. The financial statements were prepared on a modified cash basis of accounting, a comprehensive basis of accounting other than accounting principles generally accepted in the United States and is not intended to be presented in conformity with United States generally accepted accounting principles.

Internal Control Over Financial Reporting

In planning and performing my audit of the financial statements, I considered District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion in the effectiveness of the District's internal control. Accordingly, I do not express an opinion on the effectiveness of the District's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

My consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during my audit I did not identify any deficiencies in internal control over financial reporting that I consider to be material weaknesses, as defined above. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of my audit and, accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of my testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Bill Ford, C.P.A.

October 14, 2014